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The Office of Gas and Electricity Markets
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For attention of Olivia Powis

25 February 2015

Dear Olivia

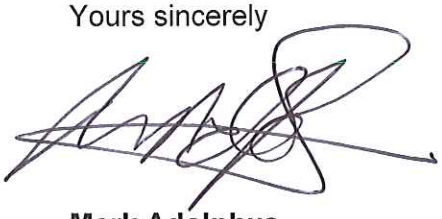
Ofgem consultation on whether the Voltage Rule should take precedence over the High Cost Cap for Distributed Generation connections

Thank you for the opportunity to respond to the above consultation. This letter should be treated as a consolidated response on behalf of UK Power Networks' three distribution licence holding companies: Eastern Power Networks plc, London Power Networks plc, and South Eastern Power Networks plc. Our response is not confidential and may be published on the Ofgem website.

Having carefully considered the proposal our view is that the High Cost Cap should take precedence over the Voltage Rule.

Our rationale for this view can be found in the appendix to this letter, however if you have any queries please do not hesitate to contact me as below.

Yours sincerely



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Appendix

Rationale for believing that the High Cost Cap should take precedence over the Voltage Rule

1. Basic principle

We disagree with Ofgem's proposal and believe that the High Cost Cap should take precedence over the Voltage Rule.

2. The existing methodology for DG customers to be treated differently is sound

We believe the rational for the High Cost Cap remains as applicable today as when it was introduced by Ofgem in 2005 under the DPCR4 arrangements. The High Cost Cap recognises the volatility and unpredictability regarding both the scale and volume of DG applications and ensures that an appropriate locational signal remains in place. We believe that the drivers for DG connections are very different to those for demand connection and that for this reason it is entirely appropriate for different charge arrangements to apply.

Where the High Cost Cap is applied it acts to ensure that costs significantly in excess of the norm are met by the connecting customer instead of being socialised across all customers.

Ofgem will be aware of the technical challenges facing DNOs for the connection of ever increasing amounts of DG. We have found that there are many areas where reinforcement of EHV and 132kV networks will be required in order to connect further DG. If precedence is given to the Voltage Rule a requirement for extensive EHV and 132kV works will result.

3. ED1 cost recovery arrangements

We are concerned that the cost allowances for ED1 are now set by Ofgem's final proposals and they do not take into account this proposed change. DNOs were not given an opportunity to reflect this change in their ED1 business plans. Furthermore, UKPN specifically reduced their proposed investment in infrastructure to support DG connections by more than £35 million. This was in part as a result of Ofgem's feedback on UKPN's draft business plan issued for consultation in November 2012. Ofgem's view, if implemented, would have significant pricing impacts. Whilst we recognise that there are re-opener mechanisms in place we believe these to provide inadequate protection in respect of the escalating load related expenditure that is likely to result.

4. The DG subsidy framework

There is risk that combined with the changing DG subsidy framework could mean that domestic customers are left to fund EHV stranded assets.

For example the recent subsidy changes make it likely for DNOs to receive more applications for 5MVA than previously and it is this level of capacity that typically may be accommodated with an 11kV point of connection. If the Voltage Rule is to take precedence then any necessary 132kV reinforcement works would normally be fully funded by the DNO (i.e. DUoS customers) and an important locational signal would be lost.

Also, DG tends to be located in rural areas where underlying load growth tends to be lower than in urban areas. Any volatility in the subsidy framework makes stranded investment more likely with again the costs falling to be met by the generality of customers.

5. Ofgem's proposal leaves the High Cost Cap in place

Notwithstanding the explanations in your letter we note that Ofgem's proposal leaves the High Cost Cap in place for DG customers. We agree that the High Cost Cap should remain in place.
If Ofgem were to agree that High Cost Cap should take precedence we do not agree that DG customers would effectively be paying deep connection charges. This would very much depend on the particular circumstances of the connection but we note that the cost apportionment factor would normally be applied up to the cap and that only costs in excess of this level would be charged in full.

6. The effect of Ofgem's proposal is not equal across Great Britain

We believe the effects of Ofgem's proposal would impact DNOs in different ways.

It is our understanding that the level of spare capacity on EHV and 132kV networks is very different across the country. In some areas large amounts of DG could be connected at the lower voltages without any EHV and 132kV reinforcement being required. However in parts of UK Power Networks areas the opposite is the case and expensive EHV and 132kV reinforcement may be triggered.

We note the current prominence of solar farm installations has greater viability in the south than in the north and this tends to coincide with low levels of spare capacity at EHV and 132kV making reinforcement more likely to be required in these areas. But the regulatory threshold arrangements for re-openers is such that a scheme in an area having a small EHV programme may prompt a re-opener whereas an equivalent value scheme in an area with a large EHV programme may not. This would cause costs to settle differently across GB including those passed on to customers generally.

7. Unintended consequences

Under Ofgem's proposal we note that the drafting of ECCR (Reg 5) would result in different charges applying dependent on the order of first and second comers.

If reinforcement is carried out more than one voltage level above the POC for a first connection such that no costs are included in connection charges, and then subsequently another customer connects at next voltage level up using the capacity created they could not be charged either. But if the second comer was to have connected first then they would have been charged a proportion of the reinforcement costs. This would be inconsistent and discriminatory charging depending on who goes first. There is a risk that it may also introduce some gaming opportunities.

8. Effects resulting from the existing arrangements

It is important to recognise that a number of DNOs currently give precedence to the High Cost Cap and that very significant amounts of DG have been connected with this interpretation in place, for UK Power Networks some 1.2GW has already been connected and with over 2.5GW in the pipeline. There is no reason to believe that this position would change if Ofgem were instead to confirm priority to the High Cost Cap for application by all DNOs.